



Attachment to AUASB Board Meeting Summary Paper

AGENDA ITEM NO.	5.3.3
Meeting Date:	10-11 September 2019
Subject:	Summary of Less Complex Entities Discussion Paper Feedback
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Date Prepared:	4 September 2019

Overview

1. As outlined in the **Agenda Item 5.3.1**, the purpose of this paper is to provide a high level summary of feedback gathered by the AUASB through the Australian LCE Survey and submissions/other comments received to assist the AUASB in developing the submission to the IAASB Discussion Paper.
2. The feedback has been separated between survey results and formal comments received. A more detailed analysis of the AUASB survey will be completed shortly and published on the AUASB's website. This analysis will also be used to support the outcomes determined in **Agenda Item 5.3.7**.
3. At a high level, the feedback the AUASB received is composed of:
 - (a) 145 responses to the AUASB LCE Survey (77% auditors); and
 - (b) 4 comment letters received/other formal communication
 - (i) KPMG Australia (**Agenda Item 5.3.4**);
 - (ii) Pitcher Partners (**Agenda Item 5.3.5**);
 - (iii) The University of Adelaide (**Agenda Item 5.3.6**); and
 - (iv) The Australian Charities and Not-for-Profits Commission.

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Question 1 – We are looking for views about how LCEs could be described (see page 4). In your view, is the description appropriate for the types of entities that would be the focus of our work in relation to audits of LCEs, and are there any other characteristics that should be included?

How should an LCE be defined?	All respondents	Auditors
A risk approach, where an LCE is defined using a range of factors such as controls and simple record-keeping	52%	50%
Entities which do not meet the current definition of a Public Interest Entity in the APESB Code	15%	17%
Size related thresholds (for example, revenue, assets, employee numbers)	33%	32%

Formal Comments	Key Themes from Feedback
KPMG Australia (KPMG)	Definition is appropriate.
Pitcher Partners (PP)	Overall, focussing on the definition is not an effective use of IAASB time. Without clarity on what the consequences of being an LCE are, it is difficult to consider what the appropriate definition should be as each jurisdiction will need to determine what is appropriate for them.
University of Adelaide (UoA)	View that the focus of the project should be shifted from the nature of the entity to the nature of the operations requiring an audit.
Australian Charities and Not-for-profits Commission (ACNC)	Whilst a number of the factors are fitting for a charity it may be difficult to clearly define/describe a LCE in the charity space due to the wide variety of charitable purposes and circumstances.

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Question 2 – Section II describes challenges related to audits of LCEs, including those challenges that are within the scope of our work in relation to audits of LCEs. In relation to the challenges that we are looking to address:

a) What are the particular aspects of the ISAs that are difficult to apply? It would be most helpful if your answer includes references to the specific ISAs and the particular requirements in these ISAs that are most problematic in an audit of an LCE.

b) In relation to 2a above, what, in your view, is the underlying cause(s) of these challenges and how have you managed or addressed these challenges? Are there any other broad challenges that have not been identified that should be considered as we progress our work on audits of LCEs?

	Total respondents		Auditors	
	Rated significant (5-7)	Rated not significant (1-3)	Rated significant (5-7)	Rated not significant (1-3)
Requirements result in certain procedures being performed solely to comply with auditing standard requirements with no additional assurance or measurable increase in audit quality	90%	8%	92%	7%
There is a lack of separate implementation support/ guidance in respect of the application of the auditing to the audit of LCEs	74%	12%	86%	7%
The auditing standards are long and voluminous	81%	11%	77%	14%
Documentation requirements are extensive and onerous	83%	9%	84%	9%
There is insufficient application or inadequate application material in the auditing standards addressing scalability and proportionality considerations	84%	19%	68%	9%
It is difficult to identify the relevant requirements for an LCE audit	71%	13%	68%	15%
There is a lack of clarity and different interpretations as to what, and how, certain matters are documented	84%	6%	71%	5%
The auditing standards are not clear about the nature and extent of work required	65%	16%	63%	17%
The language is complex and difficult to understand	61%	19%	55%	23%

Formal Comments From	Key Themes from Feedback
KPMG Australia (KPMG)	Underlying causes of the challenges are the language of the standards and lack of understanding of what is practically required for compliance and the extent of audit documentation. Heavily reliant on internally developed materials to fill this gap.

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Formal Comments From	Key Themes from Feedback
	Particular standards and aspects of the standards which are challenging for auditors of LCEs: <ul style="list-style-type: none"> - ASA 240 – journal entry testing; - ASA 315 – Understanding the entity, including internal controls and the IT environment; - ASA 500 – Information produced by a management’s expert. - ASA 540 – Extent of work for more routine estimates which are not a significant risk. - ASA 620 – Criteria for reliance on a specialist.
Pitcher Partners (PP)	Particular standards and aspects of the standards which are challenging for auditors of LCEs: <ul style="list-style-type: none"> - ASA 240 – Identification and assessment of the risks of material misstatement due to fraud. LCEs frequently have few or no RMM due to revenue recognition. (para 27) - ASA 315 – Control activities relevant to the audit. Level of documentation expected for an LCE is higher than what is appropriate. (para 21 and A107-A109). ASA 315 – Measurement and review of the entity’s financial performance. Statement in application material that there may be increased risks for smaller entities creates more work for auditors of LCEs. (para A49). ASA 315 – Audit evidence for elements of the control environment. In a smaller entity often controls are not formally documented. Difficult to meet as inquiry alone is insufficient. - ASA 330 – Substantive procedures. Testing a material balance even if there is no risk of material misstatement. (para 18) - ASA 500 – Sufficient appropriate audit evidence. Barriers to the use of technology are a significant barrier to efficient and effective LCE audits. - ASA 520 – Substantive analytical procedures. Size of the threshold is a significant factor in whether sub AR can be used for an LCE audit. (para 5(d)).

Standards	Auditor’s responses
ISA 200s	11%
ISA 315	43%
300 series of standards (excluding ISA 315)	9%
ISA 400s	4%
ISA 540	14%

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Standards	Auditor's responses
500 series of standards (excluding ISA 540)	17%
ISA 600s	1%
700 series of standards	1%
800 series of standards	3%
ISREs	1%

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Question 3 – With regard to the factors driving challenges that are not within our control, or have been scoped out of our exploratory information gathering activities (as set out in Section II), if the IAASB were to focus on encouraging others to act, where should this focus be, and why?

Formal Comments From	Key Themes from Feedback
KPMG Australia (KPMG)	IAASB should focus on: <ul style="list-style-type: none"> - Regulatory and commercial – Audit fee pressure ultimately impacts on audit quality. - Value of audit – Audits, in particular those of LCEs, are considered as a regulatory service that provides no value. - Public expectations – improving understanding of the audit process and auditor’s role.
Pitcher Partners (PP)	IAASB should focus on: <ul style="list-style-type: none"> - Tools and technology would greatly enhance audit quality and efficiency. IAASB should be amending or changing standards to allow this. - Regulatory – Regulator approach to compliance is checklist based and view guidance as mandatory. IAASB should be ensuring standards are being used appropriately by all stakeholders. - Public expectations – improving understanding of the audit process and auditor’s role, reducing the audit expectation gap.

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Question 4 – To be able to develop an appropriate way forward, it is important that we understand our stakeholders’ views about each of the possible actions. In relation to the potential possible actions that may be undertaken as set out in Section III:

- a) **For each of the possible actions (either individually or in combination):**
- a. **Would the possible action appropriately address the challenges that have been identified?**
- b. **What could the implications or consequences be if the possible action(s) is undertaken? This may include if, in your view, it would not be appropriate to pursue a particular possible action, and why.**
- b) **Are there any other possible actions that have not been identified that should be considered as we progress our work on audits of LCEs?**
- c) **In your view, what possible actions should be pursued by us as a priority, and why? This may include one or more of the possible actions, or aspects of those actions, set out in Section III, or noted in response to 4b above.**

How important do you think it is to pursue each action?	Total respondents		Auditors	
	Rated significant (5-7)	Rated not significant (1-3)	Rated significant (5-7)	Rated not significant (1-3)
Revising the auditing standards to make the auditor’s work effort clearer	75%	10%	79%	11%
Developing a separate auditing standard for audits of less complex entities	76%	17%	75%	18%
Developing guidance for auditors of less complex entities or other related actions	97%	5%	94%	4%

Basis for revising the ISAs	All respondents	Auditors
Setting out the basic requirements for all audits then expanding as needed to address more complex circumstances (building-blocks approach)	41%	42%
Including considerations specific to audits of less complex entities in a separate section within each auditing standard	30%	31%
Greater focus on more clearly setting out what the auditor needs to do	14%	14%
Featuring more scalability and proportionality considerations in the application material	12%	12%
Other (please specify)	2%	2%

Basis for developing new ISAs	All respondents	Auditors
Developing a separate auditing standard based on the existing risk-based framework	48%	45%
Developing a separate auditing standard based on a different framework (e.g. substantive testing based)	42%	46%
Other (please specify)	10%	9%

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Basis for guidance (All respondents)	All respondents	Auditors
An International Auditing Practice Note (IAPN) for Audits of Less Complex Entities	5%	5%
An enhanced comprehensive guide on applying auditing standards for audits of less complex entities	45%	46%
Focused “implementation packs” for new and revised auditing standards specifically for audits of LCEs	26%	26%
Guidance for the application of specific areas within the auditing standards or a specific auditing standard	19%	17%
Other (please specify)	4%	5%

Formal Comments From	Key Themes from Feedback
KPMG Australia (KPMG)	Revising the ISAs “building-block” approach and developing guidance. Consider that developing a separate standard would be counterproductive, increasing complexity by creating different compliance frameworks for different entities. Strongly support the adoption of a format which prescribes the minimum requirements for all types of entities and includes additional requirements for more complex entities.
Pitcher Partners (PP)	Revising the ISAs using a “building block” approach. Approach would address the issues of scalability in the audit. Setting the “minimum” requirements for an audit and developing additional guidance for more complex audits (e.g. listed entities) is within the IAASB’s powers and would likely result in compliance with ISAs through all sizes of audits. A comprehensive re-write of the standards from the ground up to address the changing auditing landscape is needed to address a number of issues such as technology, listed/non listed environment and audit expectation gap.

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Question 5 – Are there any other matters that should be considered by us as we deliberate on the way forward in relation to audits of LCEs?

Formal Comments From	Key Themes from Feedback
KPMG Australia (KPMG)	None noted.
Pitcher Partners (PP)	A building blocks approach may be more palatable than the current suggestion that “LCE” do less to obtain reasonable assurance, set the minimum requirements as the based and listed and other “special” types of entity do more with specific guidance for those types of entities to provide reasonable assurance aligning more coherently with expectations of the audit.
University of Adelaide (UoA)	View that the focus of the project should be shifted from the nature of the entity to the nature of the operations requiring an audit.
Australian Charities and Not-for-profits Commission (ACNC)	<p>Some challenges faced by the charity sector are:</p> <ul style="list-style-type: none"> - The current legislative framework sets a minimum threshold of \$1M in revenue for a mandatory audit. There is a single approach to application of standards unless a separate auditing standard for LCEs is developed whereby eligible charities could meet alternative standards (still in accordance with the Australian Auditing Standards). Should any LCE approach be formalised in Australia, the nature of such material needs to be authoritative to meet the ACNC regulatory framework. - Additional auditing requirements relating to fundraising at a state and territory level require specific audits on fundraising income and expenses. The ACNC is committed to drive and advocate for a harmonised national reporting framework for fundraising. - Impact/service performance reporting is another area that the sector appears to have particular interest in developing which may or may not require corresponding assurance. - Lack of ongoing technical resources (volunteer-based entities) or limited access to audit professionals in some remote areas. <p>We note some challenges do not fall within the remit as a standard setter and it is never an easy task to engage stakeholders to work collaboratively. Given the potential relevance and applicability to the charity sector, we see value in the LCE project progressing.</p>

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